

MULTIMEDIA



UNIVERSITY

STUDENT ID NO

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# MULTIMEDIA UNIVERSITY

## FINAL EXAMINATION

TRIMESTER 1, 2019/2020

### BAC3624 – ADVANCED AUDITING

( All sections / Groups )

12 OCTOBER 2019  
9.00 a.m. – 12.00 p.m.  
(3 Hours)

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#### INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 6 pages excluding cover page with 5 Questions only.
2. Attempt all **FIVE** questions. The distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided.

**Question 1**

(a) Your firm is the auditor of Bersatu Berhad and Perkasa Berhad.

- (i) It provides tax services to Bersatu Berhad that involves completing the tax computation and tax filing using information extracted from the company's financial statements.
- (ii) It is also the auditor of Perkasa Berhad's largest customer.

Identify and explain the potential threats to objectivity that each of the situations in (i) and (ii) above pose to your audit firm and explain the safeguards which should be in place to address them.

(4 marks)

(b) You are about to start work on an assignment. Describe your senior's roles in terms of supervising you and explaining your role in the audit.

(2 marks)

(c) Ali the senior auditor, had a serious disagreement with the Managing Director (MD) of one of his major clients. As a result, the MD has threatened to recommend another firm of auditors for an appointment at the next AGM.

Explain the powers and duties of the auditor under Section 266 of Malaysian Companies Act 2016 which the auditor has if the MD carries out his threat.

(4 marks)

(d) Iman Berhad is a civil engineering company that provides a pipe-laying service to the energy, water and telecommunications industries. It uses a significant amount of heavy plant and machinery and is subject to the strict provisions of health and safety at work regulations.

Identify the risks to which breaches of these regulations could expose the company.

(3 marks)

(e) Explain the meaning of the following terms and give examples using payroll.

- (i) Segregation of duties
- (ii) Approval and control of documents

(4 marks)

(f) Client A is a listed company. The draft profit before tax amount is RM 1 million. During the audit, the audit team requested the management to provide a written

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representation letter to confirm the management's opinion on winning or losing a particular legal case against a major supplier but the management has expressed its reluctance to provide the letter to the auditor. Explain the effects on the auditor's report. (3 marks)

**(Total : 20 marks)**

## **Question 2**

Your firm has been appointed as auditor of Sinar Bhd (Sinar), a company operating within the sports and leisure sector. Your audit manager has arranged a meeting with the company's finance director for early next week. She has asked you to assist her, in advance of this meeting to prepare the audit planning. Your audit manager has also asked you to carry out some preliminary analytical procedures on the year-end financial statements of Sinar when these become available. Sinar's business can be split into the following three divisions:

- Sports equipment retail outlets: 35 sports equipment retail outlets located in 'out of town' retail parks
- Fitness clubs: 15 fitness clubs, each offering a fully equipped gym together with yoga, aerobics and circuit training classes
- Machine manufacture: a manufacturing unit in which running machines and rowing machines are assembled using components sourced from overseas.

Further information:

### **Sports equipment retail outlets**

The retail outlets are all located close to major towns and cities throughout Malaysia. Each outlet let stocks a standard range of products which are supplied from a central warehouse operated by Sinar. Salaries for the core staff at the outlets are paid by Sinar's head office by direct bank transfer. Each outlet is run on a day-to-day basis by a manager who is responsible for hiring casual staff to cover peak periods. These casual staff members are generally paid using cash from the till.

Sinar received some bad publicity during the year following its inclusion in a television documentary which revealed that one of its sports shoe suppliers, located overseas, was making its employees work long hours for very low wages. In an attempt to manage this adverse press attention, Sinar has now had to source these products from alternative suppliers in Malaysia.

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**Fitness clubs**

Sinar's 15 fitness clubs are all located directly above existing Sinar retail outlets. Each club has its own on-site manager and is operated independently of the adjacent retail outlet.

Customers of the fitness clubs pay by one of three methods: on a 'pay per session' basis over the fitness club counter; by monthly direct debit paid into Sinar's head office bank account; or by annual subscription to head office. Customers are then issued with a membership card which enables them to gain access to the club.

The company operates a bonus incentive scheme for the managers at both its retail outlets and fitness clubs. The size of the bonus is linked to the profitability of their individual operation.

**Machine manufacture**

During the year, Sinar started to manufacture its own running machines and rowing machines. It sources the machine components from China and Taiwan. These components are assembled in Malaysia at Sinar's own factory, for sale both in Sinar's own stores under their own 'Sinar' brand and to independent sports shops under the 'Excel' brand. The latter accounts for approximately 80% of Sinar's total production of both running and rowing machines. Sales to independent sports shops achieve a gross profit margin of 50%, whereas sales to Sinar's own shops are made to that division at cost plus 10%.

Sinar is invoiced by its oversea component suppliers in their respective local currency. The components are sent by sea, which means that Sinar's typical lead time for components from the placing of an order to delivery in Malaysia is three months. Sinar is required to pay its suppliers 50% with the order and 50% upon receipt of the components in Malaysia.

**Quality control**

In line with your firm's system of quality control, procedures were conducted prior to accepting Sinar as an audit client, to ensure that it was appropriate to accept such an appointment. Your audit manager has asked you to consider the other objectives of a system of quality control and why they may be particularly relevant to Sinar.

**Required:**

(a)(i) List with reasons, the information you would require in order to carry out analytical procedures on the draft financial statements of Sinar for the year ending 30 June 2018.

(6 marks)

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- (ii) List the limitations of using analytical procedures at the planning stage of an audit. (3 marks)

(b) Identify which of the circumstances outlined above, should be taken into account when planning the audit of Sinar. Explain clearly why these matters are important and their effect on your proposed audit work. (24 marks)

**(Total : 33 marks)**

### Question 3

You are an external auditor for Frozen Berhad (Frozen), a company that sells frozen food. Frozen is negotiating a substantial contract with a supermarket chain but the supermarket is reluctant to agree to the prices and demand a 60 days credit facility. At the planning stage of the audit for the year ended 31<sup>st</sup> December 2018, the following information was also gathered.

On 1<sup>st</sup> January 2018, the managing director who was previously involved in property development acquired all the shares in Frozen from Permata Berhad, a conglomerate which was rationalising its operation. Immediately following the acquisition, Frozen had net assets of RM1 million, after taking account of low-interest loans of RM3 million from Permata Berhad. These loans are secured on the freehold property of the company and are repayable in equal quarterly instalments over a five-year period until 31<sup>st</sup> December 2023. Day-to-day working capital is funded by an overdraft facility of RM2 million, secured by a fixed and floating charge on the assets of the company. This facility is to be reviewed by the bank in 2021 after the audited accounts are available.

The original business plan envisaged the acquisition of an adjacent factory to enable the company to double its output but this expansion has been postponed. The managing director has explained that there will be a delay in preparing the draft accounts as the finance director has left and is yet to be replaced. The accountant is assisted in the day-to-day accounting function by temporary staff. There is a projected loss for the year but a forecast indicates a return to profitability in the next financial year.

#### Required:

- (a) From the situation above, identify and explain the circumstances particular to Frozen that give rise to potential financial misstatements and going concern issue. (12 marks)
- (b) Describe the procedures that you would undertake during the course of your audit in order to satisfy yourself on the status of Frozen as a going concern. (6 marks)

**(Total: 18 marks)**

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**Question 4**

Jamal & Co, an audit firm which specializes in the audit of property and service companies in Kuala Lumpur has merged with Sunny & Co which specializes in the audit of farms and holiday resorts in Sabah. The merger was seen as an opportunity for both firms to break away from their usual audit markets. Lee is a senior audit manager now working for Jamal Sunny & Co (the merged audit firm). Previously, he was working for Jamal & Co. Lee has moved from Kuala Lumpur to Sabah to take a new portfolio of clients in Kota Kinabalu and Kundasang. One of his client companies from the new portfolio is Maju Sdn Bhd which is a family business with Raju running the 90-acre farm and his eldest son, Mutu, taking responsibility for the holiday cottages, fishing lakes and preparing the accounting books and records.

The farming has been significantly decreased in recent years and now comprises a small beef herd and two geese sheds. These birds (geese) are fed on a chemical-free diet to offer a high-quality alternative to turkeys over the Christmas period. Raju supplements the farm revenue by renting his land for sheep grazing on a rotational basis to neighbouring farms. Raju is also considering the introduction of new breeds (deer and goats) to provide an additional attraction to visitors with young families. Mutu trained as a bookkeeper 20 years ago and has informed Lee that the accounts are now maintained to a high standard in his computer. This has saved a lot of time and much of the previous paperwork is now superfluous.

Five years ago, Raju borrowed a substantial sum to convert three disused barns into a luxury holiday cottage and these have proved to be a huge success, being fully booked during school holidays. During this period, two extra helpers are employed on a part-time basis to assist with cleaning and maintenance. The salaries of these two helpers are paid in cash at the end of each week.

Most of the visitors are fishermen and their families as the farm is very famous for excellent fishing. Raju is keen to maintain this quality and is always on the lookout for big fish to stock. He has recently become interested in the possibility of introducing from China some big blue carp which could be 'sneaked in' with a batch of koi carp being imported for a local garden centre.

A good relationship has always existed with the auditors thus, Raju and his son are confident that this will be another quick audit.

**Required:**

Identify from the information given above, the potential audit risks and for each risk explain why it is a risk. (20 marks)

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**Question 5**

You are doing the audit of Perdana College, a private school with approximately 2,500 students. With your firm's consultation, they have instituted an IT system that separates the responsibilities of the computer operator, systems analyst, librarian, programmer and data control group by having a different person do each function. Now, a budget reduction is necessary and one of the five people must be laid off. You are requested to give the college advice as to how the five functions could be done with reduced personnel and minimal negative effects on internal control. The amount of time the functions take is not relevant because all five people also do non-accounting functions.

**Required:**

- (a) Divide the five functions among four people in such a way as to maintain the best possible control system. (2.5 marks)
- (b) Assume that economic times become worse for Perdana College and it must terminate employment of another person. Divide the five functions among three people in such a way as to maintain the best possible internal control. The amount of time each function takes should not be a consideration in your decision. (2.5 marks)
- (c) If the five functions were done by one person, will internal controls be so inadequate that an audit cannot be done? Discuss. (4 marks)

**(Total: 9 marks)**

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